

# **EXHIBIT 6**

**THE METROPOLITAN SEWER DISTRICT  
OF GREATER CINCINNATI**

**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

for the years ended December 31, 1998 and 1997

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OF GREATER CINCINNATI**

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**Foxx & Company**  
*Certified Public Accountants*

## **INDEPENDENT AUDITORS' REPORT**

The Honorable Board of County Commissioners  
Hamilton County, Ohio

We have audited the accompanying financial statements of the Metropolitan Sewer District of Greater Cincinnati (MSD), as of and for the year ended December 31, 1998. These financial statements are the responsibility of MSD's management. Our responsibility is to express an opinion on these financial statements based on our audit. The accompanying financial statements of MSD as of and for the year ended December 31, 1997 were audited by other auditors whose report dated April 27, 1998, expressed an unqualified opinion on those statements. As discussed in Note 11, MSD has restated its 1997 financial statements during the current year to report investments at fair value, in conformity with generally accepted accounting principles. The other auditors reported on the 1997 financial statements before the restatement.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the financial position of MSD and are not intended to present fairly the financial position of Hamilton County, and the results of its operations and cash flows of its proprietary fund types and nonexpendable trust funds in conformity with generally accepted accounting principles.

We also audited the adjustment described in Note 11 that was applied to restate the 1997 financial statements. In our opinion, the adjustment is appropriate and has been properly applied.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Metropolitan Sewer District of Greater Cincinnati, at December 31, 1998, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued a report dated May 5, 1999 on our consideration of MSD's internal control over financial reporting and out tests of its compliance with certain provisions of laws, regulations, contracts and grants.

The Year 2000 Supplementary Information on page 20 is not a required part of the financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplemental information. However, we did not audit the information and do not express an opinion on it. In addition, we do not provide assurance that the MSD is or will become year 2000 compliant, that the MSD's year 2000 remediation efforts will be successful in whole or in part, or that parties with which the MSD does business are or will become year 2000 compliant.

In addition, we did not audit the introductory and statistical information listed in the table of contents. Accordingly, we express no opinion on such data.

*Fox & Company*

Cincinnati, Ohio  
May 5, 1999

## THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI

## BALANCE SHEETS

December 31, 1998 and 1997

(all amounts expressed in thousands)

## ASSETS

	<u>1998</u>	<u>1997</u>
<b>Current Assets</b>		
Cash and cash equivalents held by the City of Cincinnati	\$ 11,108	\$ 11,841
Accounts receivable	16,539	17,399
Prepaid expenses and other	<u>2,297</u>	<u>2,452</u>
Total current assets	<u>29,944</u>	<u>31,692</u>
<b>Restricted Assets</b>		
Cash and cash equivalents held by the City of Cincinnati		
Construction account	5,062	9,115
Amount to be transferred to surplus account	9,824	14,235
Held by trustee		
Cash and cash equivalents	12,867	1,831
Investments - Held to maturity	<u>127,599</u>	<u>146,726</u>
Total restricted assets	<u>155,352</u>	<u>171,907</u>
<b>Property, Plant and Equipment</b>		
Land	4,925	4,925
Building and structures	544,995	533,684
Processing systems	218,974	216,678
Office and service equipment	23,065	22,381
Construction in progress	<u>105,259</u>	<u>73,099</u>
Total property plant and equipment	897,218	850,767
Accumulated depreciation	<u>(299,363)</u>	<u>(275,911)</u>
Net property, plant and equipment	<u>597,855</u>	<u>574,856</u>
<b>Other Assets</b>		
Unamortized financing costs	7,789	8,402
Other	<u>2,957</u>	<u>3,145</u>
Total other assets	<u>10,746</u>	<u>11,547</u>
Total assets	<u>\$793,897</u>	<u>\$790,002</u>

The notes to the financial statements are an integral part of the financial statements.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**BALANCE SHEETS**

**December 31, 1998 and 1997**  
**(all amounts expressed in thousands)**

**LIABILITIES AND EQUITY**

	<u>1998</u>	<u>1997</u>
<b>Current Liabilities</b>		
Current portion of long-term debt	\$ 13,737	\$ 13,132
Accounts payable	2,977	4,546
Accrued payroll expenses	<u>1,482</u>	<u>1,430</u>
Total current liabilities	<u>18,196</u>	<u>19,108</u>
<b>Payable From Restricted Assets</b>		
Construction accounts payable	9,458	3,351
Accrued interest	<u>1,657</u>	<u>1,704</u>
Total payable from restricted assets	<u>11,115</u>	<u>5,055</u>
<b>Long-Term Liabilities</b>		
Accrued compensated absences	5,737	5,451
Long-term debt (Net of deferred loss on refunding bonds of \$314 in 1998 and \$444 in 1997)	<u>378,839</u>	<u>392,170</u>
Total long-term liabilities	<u>384,576</u>	<u>397,621</u>
Total liabilities	<u>413,887</u>	<u>421,784</u>
<b>Equity</b>		
Contributions in aid of construction	170,650	170,626
Retained earnings	<u>209,360</u>	<u>197,592</u>
Total equity	<u>380,010</u>	<u>368,218</u>
Total liabilities and equity	<u>\$793,897</u>	<u>\$790,002</u>

The notes to the financial statements are an integral part of the financial statements.



**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**STATEMENTS OF REVENUES, EXPENSES**  
**AND CHANGES IN FUND EQUITY**  
**for the years ended December 31, 1998 and 1997**  
**(all amounts expressed in thousands)**

	<u>1998</u>	<u>1997</u>
<b>Operating Revenues</b>		
Sewerage service charges	\$ 89,837	\$ 88,504
Sewerage surcharges	10,128	11,422
Other revenues	<u>2,889</u>	<u>2,462</u>
Total operating revenues	<u>102,854</u>	<u>102,388</u>
<b>Operating Expenses</b>		
Personnel services	34,246	35,397
Utilities, fuel and supplies	13,114	14,160
Depreciation and amortization	25,096	23,859
Purchased services	15,656	16,192
Other expenses	<u>3,589</u>	<u>3,829</u>
Total operating expenses	<u>91,701</u>	<u>93,437</u>
Income from operations	<u>11,153</u>	<u>8,951</u>
<b>Other Income (Expenses)</b>		
Interest income	9,083	5,938
Gain (loss) on disposal of property, plant and equipment	41	(49)
Interest expense	(18,136)	(16,367)
Net increase in fair value of investments	<u>1,475</u>	<u>1,513</u>
Total other income (expense)	<u>(7,537)</u>	<u>(8,965)</u>
<b>Net Income (Loss)</b>	3,616	(14)
Amortization of contributions in aid of construction	8,152	7,893
Retained earnings at beginning of year, restated (Note 11)	<u>197,592</u>	<u>189,713</u>
Retained earnings at end of year	<u>209,360</u>	<u>197,592</u>
Contributions in Aid of Construction at beginning of year	170,626	173,173
Additions to contributions in aid of construction	8,176	5,346
Amortization of contributions in aid of construction	<u>(8,152)</u>	<u>(7,893)</u>
Contributions in aid of construction at end of year	<u>170,650</u>	<u>170,626</u>
<b>Total Fund Equity at End of Year</b>	<u>\$380,010</u>	<u>\$368,218</u>

The notes to the financial statements are an integral part of the financial statements.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**STATEMENTS OF CASH FLOWS**  
**for the years ended December 31, 1998 and 1997**  
**(all amounts expressed in thousands)**

	<u>1998</u>	<u>1997</u>
<b>Cash Flows from Operating Activities</b>		
Cash received from customers	\$100,825	\$ 101,562
Cash payments for goods and services	(33,984)	(33,216)
Cash payments for personnel costs	(33,908)	(35,263)
Other operating revenues	<u>3,123</u>	<u>4,596</u>
<b>Net Cash Provided by Operating Activities</b>	<u>36,056</u>	<u>37,679</u>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Proceeds from sale of revenue bonds	-	105,245
Revenue bonds issuing cost	-	(387)
Principal and interest payments on long-term debt	(34,348)	(26,457)
Acquisition and construction of capital assets	(37,253)	(42,185)
Grant and loan proceeds	910	4,612
Tap-in fees	4,653	3,018
Proceeds from sale of property, plant and equipment	<u>81</u>	<u>80</u>
<b>Net Cash Provided (Used) by Capital and Related Financing Activities</b>	<u>(65,957)</u>	<u>43,926</u>
<b>Cash Flows from Investing Activities</b>		
Purchase of government securities	(91,260)	(382,955)
Maturity or redemption of government securities	111,862	303,773
Interest earned on investments	<u>11,138</u>	<u>5,733</u>
<b>Net Cash Provided (Used) by Investing Activities</b>	<u>31,740</u>	<u>(73,449)</u>
<b>Net Change in Cash and Cash Equivalents</b>	1,839	8,156
<b>Cash and Cash Equivalents at January 1</b>	<u>37,022</u>	<u>28,866</u>
<b>Cash and Cash Equivalents at December 31</b>	<u><u>\$ 38,861</u></u>	<u><u>\$ 37,022</u></u>
<b>Reconciliation of Operating Income to Net Cash Provided by Operating Activities:</b>		
Income from operations	\$ 11,153	\$ 8,951
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	25,096	23,859
Change in assets and liabilities:		
Allowance for doubtful accounts	400	280
Net change in customer accounts receivable	460	1,356
Net change in other assets	193	2,129
Net change in operating accounts payable	(1,584)	970
Net change in accrued payroll and related expenses	<u>338</u>	<u>134</u>
<b>Net Cash Provided by Operating Activities</b>	<u><u>\$ 36,056</u></u>	<u><u>\$ 37,679</u></u>
<b>Noncash Investing and Financing Transactions</b>		
Assets received for settlement receivable	\$ 225	\$ -
Structures donated as contributed capital in aid of construction	<u>2,623</u>	<u>1,999</u>
<b>Total Noncash Investing and Financing Transactions</b>	<u><u>\$ 2,848</u></u>	<u><u>\$ 1,999</u></u>

The notes to the financial statements are an integral part of the financial statements.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
NOTES TO THE FINANCIAL STATEMENTS  
for the years ended December 31, 1998 and 1997**

**NOTE 1 - ACCOUNTING POLICIES**

A summary of the significant accounting policies applied in the accompanying financial statements follows:

**Organization**

The Metropolitan Sewer District of Greater Cincinnati (MSD), an enterprise fund of the County of Hamilton, Ohio, collects and treats industrial and residential wastewater for municipalities and unincorporated areas of Hamilton County. MSD was established pursuant to an agreement dated May 1, 1968 between the Board of Commissioners of Hamilton County and the City of Cincinnati. Under a contract with the City of Cincinnati, the Board designated the City as its agent for the maintenance and operation of MSD. The annual budget, prepared on the cash basis of accounting, is approved by the Board and administered by the City. Budgetary control is exercised at the divisional level, and between personnel and all other costs. The County issues a separate Comprehensive Annual Financial Report which includes MSD as a separate enterprise fund of the County.

**Basis of Accounting**

The accompanying financial statements were prepared on the accrual basis of accounting, whereby revenues and expenses are recognized in the period earned or incurred.

**Enterprise Fund Activity Accounting and Financial Reporting**

Enterprise funds and similar component units apply Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict Governmental Accounting Standards Board (GASB) pronouncements, in which case, GASB prevails.

**Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## **Statement of Cash Flows**

For purposes of the Statements of Cash Flows, all highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents.

## **Investments**

MSD is required by Ohio law to invest in only United States obligations; federal agency securities; Ohio bonds and other obligations or such obligations of political subdivisions of the state, provided that the subdivisions are located within Hamilton County; time certificates of deposit or deposit accounts in an eligible institution; and no load money market mutual funds consisting only of investments mentioned above. Investments are required to mature within five years from the date of settlement, unless the investment is matched to a specific obligation or debt of MSD.

Investment securities are stated at fair value in accordance of GASB Statement No. 31.

## **Inventory**

Supplies and materials are stated at the lower cost or market on a first-in, first-out (FIFO) basis.

## **Property, Plant and Equipment**

Property, plant and equipment are stated at historical cost for assets acquired after MSD's inception in 1968. Assets which were acquired prior to 1968 and not identifiable with specific historical costs are not included in the property, plant and equipment balance. Assets acquired by MSD through contributions, such as contributions from land developers and federal and state grants, are capitalized and recorded in the plant records at the contributors' reported cost. Construction costs include interest capitalized on debt during the period of construction and the cost of in-force labor.

Depreciation expense is computed on the straight-line method over the estimated useful lives of the respective assets. The estimated lives are as follows:

Building and structures	40 years
Processing systems	25 years
Office and service equipment	5-15 years

Depreciation expense on property, plant and equipment acquired through contributions is reported as an offset against contributions in aid of construction in fund equity. Any gain or loss arising from the disposal of property, plant and equipment has been credited or charged to income.

### **Unamortized Financing Costs**

The unamortized financing costs include bond discount, consulting and attorney fees incurred in connection with the revenue bond obligations. These amounts are being amortized on the interest method and the straight-line method, respectively, over the lives of the revenue bonds.

### **Pension Plans**

Employees participate in either the City of Cincinnati's Retirement System or the Public Employees Retirement System administered by the State of Ohio. Pension costs reflect a percentage of employees' gross pay, as defined by the terms of pension plans in which employees participate. MSD's policy is to fund pension costs accrued.

### **Claims Liabilities**

MSD records an estimated liability for indemnity health care, workers' compensation, torts and other claims against them. Claims liabilities are based on estimates of the ultimate cost of reported claims (including future claim adjustment expenses) and an estimate for claims incurred but not reported based on historical experience claims liabilities include specific, incremental claim adjustment expenses, allocated loss adjustment expenses, and are reduced for estimated recoveries on unsettled claims such as salvage or subrogation.

### **Compensated Absences**

Compensated absences are accrued in accordance with GASB Statement No. 16. Components of the liability include accrued vacation time, sick leave, compensatory time and other related payments.

## **NOTE 2 - DEPOSITS AND INVESTMENTS**

The following information classifies deposits and investments by category of risk as defined in GASB Statement No. 3, "Deposits with Financial Institutions, Investments and Repurchase Agreements"

*Deposits:* At December 31, 1998 and 1997, the carrying amount of MSD's deposits held by the City of Cincinnati total \$25,994,000 and \$35,191,000, respectively. Amounts held by the City of Cincinnati are invested on MSD's behalf in accordance with the Cincinnati Municipal Code. Amounts held by the City are collateralized as part of the City's cash and investment balances.

*Investments:* Funds held by trustees are eligible investments as defined by the Trust Agreement and are in the name of the trustee for the benefit of MSD.

Investments made by MSD are summarized below. Trustee account investments are categorized according to credit risk into the following categories: (1) insured or registered, or securities held by MSD's or its agent (bank trust department) in the MSD's name; or (2) uninsured and unregistered,

with securities held by the counterparty's trust department or agent in the MSD's name; or (3) uninsured, unregistered securities held by the counterparty, or its trust department or agent but not in MSD's name. Money market funds are unclassified investments since they are not evidenced by securities that exist in physical or book entry form.

(all amounts in thousands)

	<u>Category</u>			<u>Carrying Amount</u>	<u>Fair Value</u>
	<u>1</u>	<u>2</u>	<u>3</u>		
<u>December 31, 1998</u>					
U.S. Government Securities	\$127,599	\$ -	\$ -	\$127,599	\$127,599
Money Market Funds	<u>-</u>	<u>-</u>	<u>-</u>	<u>12,867</u>	<u>12,867</u>
Total	<u>\$127,599</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$140,466</u>	<u>\$140,466</u>

December 31, 1997

U.S. Government Securities	\$146,726	\$ -	\$ -	\$146,726	\$146,726
Money Market Funds	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,831</u>	<u>1,831</u>
Total	<u>\$146,726</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$148,557</u>	<u>\$148,557</u>

The classification of cash and cash equivalents and investments on the financial statements is based on criteria set forth in GASB Statement No. 9. A reconciliation between the classifications of cash and investments on the financial statements and the classification per GASB Statement No. 3 is as follows:

(all amounts in thousands)

<u>December 31, 1998</u>	<u>Cash and Cash Equivalents</u>	<u>Investments</u>
GASB Statement No. 9	\$38,861	\$127,599
Money Market Funds	<u>(12,867)</u>	<u>12,867</u>
GASB Statement No. 3	<u>\$25,994</u>	<u>\$140,466</u>
 <u>December 31, 1997</u>	 <u>Cash and Cash Equivalents</u>	 <u>Investments</u>
GASB Statement No. 9	\$37,022	\$146,726
Money Market Funds	<u>(1,831)</u>	<u>1,831</u>
GASB Statement No. 3	<u>\$35,191</u>	<u>\$148,557</u>

Accounts receivable consist of the following:

(all amounts in thousands)		<u>December 31,</u>	
		<u>1998</u>	<u>1997</u>
Sewerage charges and surcharges:			
Unbilled amount		\$ 8,905	\$ 9,168
Billed amount		8,540	8,692
Less allowance for doubtful accounts		(1,900)	(1,500)
Other		<u>994</u>	<u>1,039</u>
Total		<u>\$16,539</u>	<u>\$17,399</u>

#### **NOTE 4 - RESTRICTIONS ON ASSETS**

Land acquired for MSD's use is titled to either the City of Cincinnati or Hamilton County. The cost of this land has been recorded on the books of MSD since it has the full benefit of the land as an economical resource.

In August 1985, the Federal District Court entered a consent order in an action with MSD and others (see Commitments and Contingencies Note). In complying with the consent order, MSD is required to maintain amounts on deposit in an environmental security account. Expenditures from this account must be approved by the U.S. Environmental Protection Agency. The balance of this account, which is included in other assets, was \$993,000 and \$947,000 at December 31, 1998 and 1997, respectively.

The Trust Agreement for the Series A Revenue Bonds (see Long-Term Debt Note) requires the establishment of certain trust accounts including a Bond Account, Bond Reserve Account, Replacement and Improvement Account, and a Surplus Account to be held by the Trustee. The Bond Account will be used to accumulate periodic principal and interest payments. The Bond Reserve Account will be funded in an amount equal to the highest annual future debt service requirement. The Surplus Account is available to be used for any other Sewer System purpose. The Trust Agreement also requires the creation of a Construction Account to be held by the City to pay for project costs. At December 31, 1998 and 1997 the following balances were maintained in the trust accounts:

(all amounts in thousands)		<u>December 31,</u>	
		<u>1998</u>	<u>1997</u>
Held by trustee:			
Reserve		\$ 35,551	\$ 33,902
Replacement and improvement		4,972	4,956
Expense fund		-	26
Bond retirement		3,129	3,069
Surplus		<u>96,814</u>	<u>106,604</u>
Total		<u>\$140,466</u>	<u>\$148,557</u>

**NOTE 5 - LONG-TERM DEBT**

Long-term debt consisted of the following:

(all amounts in thousands except percents)

	<u>Principal Issue</u>	<u>Interest Rate</u>	<u>Year of Maturity</u>	<u>December 31,</u>	
				<u>1998</u>	<u>1997</u>
Series A Revenue Bonds					
1997	\$105,245	3.85-5.14	2017	\$101,975	\$105,245
1995	85,800	3.70-6.05	2017	79,090	81,660
1993	171,790	2.45-5.60	2016	164,570	165,415
1991	90,950	4.80-6.70	2013	28,890	33,495
Loveland Sewer District	200	5.75	2000	20	30
Ohio Water Development Authority Contracts	41,830	2.00-7.49	2019	4,823	5,953
Ohio Water and Sewer Rotary Commission	-	-	-	124	124
Ohio Public Works Commission	-	3.54-4.80	2017	3,001	3,091
Water Pollution Control Loan Fund	-	0.00-3.00	2018	10,397	10,710
Capital Lease	293	7.35	1998	-	23
 Total obligations				392,890	405,746
 Less current maturities				<u>(13,737)</u>	<u>(13,132)</u>
 Long-term portion				379,153	392,614
 Less deferred loss on refunding				<u>(314)</u>	<u>(444)</u>
 Long-term portion				<u>\$378,839</u>	<u>\$392,170</u>

Principal payments on long-term debt for the next five years and thereafter are as follows:

(all amounts in thousands)

1999	\$ 13,737
2000	14,416
2001	14,776
2002	14,936
2003	15,578
Thereafter	<u>319,447</u>
Total	<u>\$392,890</u>



**Series A Revenue Bonds**

Effective October 22, 1997, MSD issued \$105,245,000 County of Hamilton, Ohio 1997 Series A Sewer System Improvement Revenue bonds dated October 1, 1997. The proceeds from the 1997 bonds were used to permanently fund certain previous expenditures, fund the new bond reserve requirement and pay the cost of issuance. The 1997 bonds are special obligations of the District, payable solely from the net revenues of the District and are issued on a parity with the 1991, 1993, and 1995 Series A bonds, secured equally and ratably under the Trust Agreement.

Effective August 31, 1995, MSD issued \$85,800,000 county of Hamilton, Ohio 1995 Series A Sewer System Improvement and Refunding Revenue bonds dated August 15, 1995. The proceeds from the 1995 bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1986 and 1991 Series A bond issues, fund the new bond reserve requirement and pay the cost of issuance. The 1995 bonds are special obligations of the District payable solely from the net revenues of the District and are issued on a parity with the 1991 and 1993 Series A bonds, secured equally and ratably under the Trust Agreement.

Effective May 4, 1993, MSD issued \$171,790,000 county of Hamilton, Ohio 1993 Series A Sewer System Improvement and Refunding Revenue bonds dated April 15, 1993. The proceeds from the 1993 Bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1986 and 1991 Series A bond issues, fund the new bond reserve requirement, and pay the cost of issuance. The 1993 bonds are special obligations of the District payable solely from the net revenues of the District and are issued on a parity with the 1991 Series A bonds, secured equally and ratably under the Trust Agreement.

Effective February 26, 1991, MSD issued \$90,950,000 County of Hamilton, Ohio, 1991 Series A Sewer System Improvement and Refunding Revenue Bonds dated January 15, 1991. The proceeds from the 1991 Bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1985 Series A bond issue, fund the new bond reserve requirement, and pay the cost of issuance.

The 1997, 1995, 1993 and 1991 Bonds may be redeemed prior to their maturities in accordance with provisions of the bond resolutions. The redemption process for the bonds include declining premiums up to 3 percent of principal.

Maturities for bonds over the next five years and thereafter are shown below.

(all amounts in thousands)

	<b><u>1997</u></b> <b><u>Bonds</u></b>	<b><u>1995</u></b> <b><u>Bonds</u></b>	<b><u>1993</u></b> <b><u>Bonds</u></b>	<b><u>1991</u></b> <b><u>Bonds</u></b>
1999	\$ 3,420	\$ 2,685	\$ 885	\$ 4,875
2000	3,570	2,800	930	5,175
2001	3,730	5,095	975	3,325
2002	3,900	3,920	2,440	3,530
2003	4,075	4,160	2,565	3,750
Thereafter	<u>83,280</u>	<u>60,430</u>	<u>156,775</u>	<u>8,235</u>
	<u>\$101,975</u>	<u>\$79,090</u>	<u>\$164,570</u>	<u>\$28,890</u>

Under the terms of the amended revenue bond trust indenture, MSD has agreed to certain covenants, among other things, to restrict additional borrowing, maintain rates sufficient to meet debt service requirements, and maintain specified fund balances under trust agreements.

The Revenue Serial bond issues as discussed above contain covenants which require the MSD to maintain a level of debt service coverage. The following calculation reflects MSD's debt service coverage.

(all amounts in thousands except percents)

	<b><u>1998</u></b>	<b><u>1997</u></b>
Revenues:		
Total operating revenues	\$102,854	\$102,388
Interest income	9,083	5,938
Capitalized interest income	1,905	569
Tap-in/connection fees	<u>4,653</u>	<u>3,018</u>
Total pledged revenues	118,495	111,913
Total operating and maintenance expenses		
less depreciation and amortization	(66,605)	(69,578)
Half of pledged revenues transferred		
to surplus account	<u>4,912</u>	<u>7,118</u>
Net income available for debt service (a)	<u>\$ 56,802</u>	<u>\$ 49,453</u>
Principal and interest requirements on revenue bonds (b)	<u>\$ 31,743</u>	<u>\$ 23,886</u>
Principal and interest requirements on all obligations (c)	<u>\$ 34,326</u>	<u>\$26,083</u>
Debt service coverage:		
Revenue Bonds (a) divided (b)	<u>179%</u>	<u>207%</u>
All obligations (a) divided (c)	<u>165%</u>	<u>190%</u>
Basic coverage required on bonds	<u>125%</u>	<u>125%</u>

### **Loveland Sewer District**

Sewer Improvement Bonds in the amount \$200,000 were issued by the City of Loveland in 1974. MSD assumed this debt upon merger of the Loveland Sewer District into MSD in March, 1985.

### **Ohio Water Development Authority Contracts**

All contracts between the Ohio Water Development Authority (OWDA) and the Metropolitan Sewer District require MSD to prescribe and charge such rates for sewer usage which are sufficient (after expenses of operation and maintenance) to pay principal and interest on OWDA contracts. The principal is repayable in equal semi-annual installments to maturity.

### **Ohio Water and Sewer Rotary Commission**

Advances from Ohio Water and Sewer Rotary Commission represent tap-in fees and acreage assessments to be forwarded to the Commission upon collection from customers. Such advances do not bear interest unless they are determined to be in default.

### **Ohio Public Works Commission**

The MSD has entered into agreements with the Ohio Public Works Commission (OPWC) for financing of certain qualified capital projects. As the projects progress the commitments are drawn down as funds are paid by OPWC directly to the contractors. The principal is repayable in semi-annual installments to the date of maturity for each project.

### **Water Pollution Control Loan Fund**

The MSD has received low interest loan commitments from the Ohio Water Pollution Control Loan fund for certain qualified projects. As the projects progress the commitments are drawn down.

### **Capital Lease**

A five year lease/purchase agreement for communication equipment commenced in 1993 with monthly payments of \$4,661 to 1998.

**Interest on Long-Term Obligations**

The following interest costs were incurred and expensed or capitalized as part of the cost of MSD's additions to property, plant, and equipment.

(all amounts in thousands)

	<u>1998</u>	<u>1997</u>
Interest incurred	\$21,913	\$17,971
Less interest capitalization	<u>(3,777)</u>	<u>(1,604)</u>
Interest expense	<u>\$18,136</u>	<u>\$16,367</u>

**NOTE 6 - DEFEASED DEBT****Other Defeasance**

In prior years, MSD defeased various general obligation serial bonds and revenue serial bonds through refinancing and operations. Separate irrevocable trust funds were established and funded to fully service the defeased debt until the debt is called or matures. For financial reporting purposes, the debt has been considered defeased and is not included in the financial statements. At December 31, 1998 and 1997, the amount of defeased debt outstanding amounted to \$44,420,000 and \$45,421,000, respectively.

**NOTE 7 - CONTRIBUTIONS IN AID OF CONSTRUCTION**

Contributions have been received from the OWDA and the United States Government in accordance with agreements transacted between MSD and these two entities. The City of Cincinnati and Hamilton County provided working capital to MSD upon formation, and those capital contributions are included in the amounts below. Other contributions have been received in connection with the expansion of sewerage services.

Net contributions in aid of construction consisted of the following:

(all amounts in thousands)

	<u>December 31,</u>	
	<u>1998</u>	<u>1997</u>
United States Government Grants	\$129,722	\$129,722
City of Cincinnati	68,356	68,356
Ohio Water Development Authority Grants	46,761	46,197
Customers	81,491	73,879
Hamilton County	<u>1,738</u>	<u>1,738</u>
	328,068	319,892
Less accumulated amortization of contributions in aid of construction	<u>(157,418)</u>	<u>(149,266)</u>
	<u>\$170,650</u>	<u>\$170,626</u>

**NOTE 8 - PENSION AND RETIREMENT**

A limited number of MSD employees participate in the Public Employee' Retirement System administrated by the State of Ohio. PERS is not material to the financial statements of MSD and additional disclosures concerning PERS, including other postemployment benefit information, can be found in the plan's annual financial statements. Interested parties may obtain a copy by written request to 277 East Town Street, Columbus, Ohio 43215-4642.

**City of Cincinnati Retirement System**

The majority of MSD full-time employees participate in the Retirement System of the City of Cincinnati (CRS). CRS is a cost-sharing, multiple-employer, defined benefit, public employee retirement system. The plan provides retirement, disability and death benefits to plan members and beneficiaries. CRS also provides health care benefits to vested retirees. Benefits provided under the plan are established by the Cincinnati Municipal Code. CRS issues a separate, publicly available financial report that includes financial statements and required supplementary information. That report may be obtained from the City of Cincinnati Retirement System, 801 Plum Street, Cincinnati, Ohio 45202 or by calling (513) 352-3227.

The Cincinnati Municipal Code provides statutory authority for employee and employer contribution rates. For 1998, the required, actuarially determined contribution rates are 14 percent for MSD and 7 percent for employees. MSD's contributions to CRS for the years ending December 31, 1998, 1997 and 1996 were \$3,687,000, \$5,095,000 and \$5,223,000, respectively, equal to the required contribution for each year.

**Other Postemployment Benefit Information**

CRS provides hospital and surgical insurance to retired members who have earned fifteen years credited service at the time of termination or terminate after age sixty with five years credited service. Those who are receiving survivor benefits of eligible members are entitled to have their hospital and surgical insurance premiums paid by the CRS. When benefits would be reduced by reason of the retired member's eligibility for hospital and medical benefits under federal social security laws, CRS will pay whatever additional fees are required for the Federal medical coverage.

The health care coverage provided by the CRS is advance-funded on an actuarial determined basis as a portion of the employer contribution requirement to the System. The Cincinnati Municipal Code provides authority for employer contributions. Health care coverage has been included in the calculation of the pension benefit obligation, and assets and liabilities are not separately determined.

The actuarial assumptions used for the December 31, 1998 valuation of unfunded liabilities included an assumption recognizing medical benefits at current premium costs with projected increases of 7 percent per annum. The cost of coverage is recognized as an expense as claims are paid.

CRS has 5,896 active contributing participants of which 635 are MSD employees. For 1998 MSD's contribution was 17 percent of the total employer contribution.

**NOTE 9 - RELATED PARTY TRANSACTIONS**

Cincinnati Water Works provides billing and collection services on customers' accounts for MSD. Fees for these services for 1998 and 1997 were \$3,535,000 and \$3,292,000 respectively. Fees are also paid to other municipalities and villages within Hamilton County for collection of sewerage bills.

The City of Cincinnati provides "overhead" services to MSD, such as check disbursement, investment and legal services, etc. The fees for these services for 1998 and 1997 were \$1,673,000 and \$2,289,000 respectively. In addition, the City's Municipal Garage provides gasoline and repairs vehicles for MSD. Fees for these services were \$820,000 and \$877,000 for 1998 and 1997, respectively.

**NOTE 10 - COMMITMENTS AND CONTINGENCIES**

The City of Cincinnati and the Board of County Commissioners of Hamilton County, Ohio, are parties to a Federal Consent Order which was entered in settlement of United States of America vs. The Board of County Commissioners of Hamilton, County, Ohio et al., Case No. C-1-85-0693. The City and County have continued in their efforts to negotiate an amendment to change certain construction schedules appearing in exhibits to that order. The City and County believe these changes are due to circumstances beyond the control of either, and are seeking approval of those schedule modifications from the United States Environmental Protection Agency. The consent order provides for stipulated penalties for failure to meet certain construction schedule deadlines but specifically contemplates that no such penalties will be collected from either defendant where the non-compliance was beyond the reasonable control of the defendants. In addition, according to MSD's Chief Legal Counsel, EPA has requested the payment of \$290,000 in stipulated penalties under the Consent Order for certain effluent limit excursions between 1988 and January 1, 1991. The Consent order provides for stipulated penalties under certain conditions, and although the City and County have argued that no substantial penalties are appropriate, it appears that EPA does intend to extract some monetary payment for excursions. Currently, the City is awaiting EPA's response to certain defenses presented during 1992. The EPA has also claimed additional stipulated damages are appropriate for exceedences at the Mill Creek Plant, sanitary sewer overflows, and other MSD facilities at various times since January 1, 1991. Currently the EPA and the Justice Department are seeking to negotiate a new Consent Order to replace the initial Order which deals with a wider range of issues, including the Mill Creek Plant, sanitary and combined sewer overflows, and a number of other components of the wastewater collection and treatment system. Concurrently, with these negotiations the City and County are negotiating with federal and state agencies for an administrative order dealing with existing sanitary sewer overflow issues in the wastewater collection system.

As part of MSD's capital improvement program, MSD has entered into a number of contracts for construction, design, and other services. Commitments under these contracts aggregate approximately \$50 million as of December 31, 1998.

**NOTE 11 - CHANGE IN ACCOUNTING PRINCIPLE AND RECLASSIFICATIONS**

For 1998, MSD has implemented GASB Statement No. 31 of the Governmental Accounting Standards Board, "Accounting and Financial Reporting for Certain Investments and External Investment Pools." Statement No. 31 established new valuations standards for certain investments and new accounting and financial reporting standards for all investments held by external investment pools. The implementation of this statement required restatements to opening fund equity. Adjustments have been made to the January 1, 1997 retained earnings balance and 1997 activities have been restated.

The adjustments to retained earnings as of January 1, 1997 are as follows:

(all amounts in thousands)

Retained Earnings at January 1, 1997 as previously reported	\$190,284
Cumulative effect of change in accounting principle	<u>(571)</u>
Retained Earnings at January 1, 1997, as restated	<u>\$189,713</u>

The effect of the adjustments on the net loss for the year ended December 31, 1997 is to reduce the amount previously reported as a net loss by \$1,645,000.

In addition, various amounts previously reported for the year ended December 31, 1997 have been reclassified to conform with 1998 classifications.



**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
REQUIRED SUPPLEMENTAL INFORMATION  
December 31, 1998**

**Year 2000 ISSUE**

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely affect MSD's operations as early as fiscal year 1999.

The year 2000 issue is the result of using only the last two digits to indicate the year in computer hardware and software and in embedded technology. Certain programs do not properly recognize a year that begins with "20". If uncorrected, such programs will be unable to interpret dates beyond the year 1999, which could cause computer system failure or other errors, disrupting normal business operations.

MSD started addressing the year 2000 issue in late 1997. An inventory has been completed of computer systems and other equipment necessary to conducting District operations. Because the District is operated by the City of Cincinnati, many of the support systems utilized by the District such as billing, financial, personnel, purchasing, are part of the City's overall system. The City has completed its year 2000 inventory and is executing a plan for solutions to meet year 2000 compliance.

MSD is systematically upgrading hardware and software to achieve year 2000 compliance. The cost of the endeavor is difficult to distinguish from the normal upgrade and replacement process that occurs each year. The internal costs for this project are principally the related payroll costs associated with working on the year 2000 issue and is not separately tracked. Suppliers of goods and services are being contacted on an on-going basis for their year 2000 compliance status and assurance as it affects MSD. MSD is running tests on mission critical processes to determine year 2000 compatibility and where necessary taking corrective measures. Most critical plant operations could, if necessary, be performed manually. MSD in addressing the year 2000 issue is also making contingency plans such as additional personnel for critical operations and troubleshooting, back-up of various data bases, back-up power sources, adequacy of critical supplies, and checklists of options.

Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determined until the year 2000 and thereafter. MSD cannot assure that MSD is or will be year 2000 ready, that MSD's remediation efforts will be successful in whole or in part, or that parties with whom MSD does business will be year 2000 ready.





**Foxy & Company**  
Certified Public Accountants

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS  
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

The Honorable Board of County Commissioners  
Hamilton County, Ohio

We have audited the financial statements of The Metropolitan Sewer District of Greater Cincinnati (MSD), Hamilton County, Ohio, as of and for the year ended December 31, 1998, and have issued our report thereon dated May 5, 1999. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Compliance**

As part of obtaining reasonable assurance about whether MSD's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered MSD's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information and use of management and is not intended to be and should not be used by anyone other than these specified parties.

*Fox & Company*

Cincinnati, Ohio  
May 5, 1999

